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Nos. 84-871, 84-889, 84-1054 and 84-1069

In the Supreme Court of the United States

OCTOBER TERM, 1985

LOUISIANA PUBLIC SERVICE COMMISSION,
Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION
and UNITED STATES OF AMERICA, et al.,
Respondent.

(and three related cases)

ON WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF
APPEALS FOR THE FOURTH CIRCUIT

MOTION FOR LEAVE TO FILE AND BRIEF OF THE TELEPHONE RATEPAYERS ASSOCIATION FOR COST-BASED AND EQUITABLE RATES AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

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The United States Court of
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**MOTION OF
THE TELEPHONE RATEPAYERS ASSOCIATION FOR
COST-BASED AND EQUITABLE RATES
FOR LEAVE TO FILE BRIEF AS AMICUS CURIAE**

The Telephone Ratepayers Association for Cost-based and Equitable Rates (TRACER) respectfully requests leave of the Court to file the attached brief as amicus curiae in support of petitioners.[1] As grounds for its motion, TRACER states as follows.

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[1] Pursuant to Rule 42(2) of the Supreme Court Rules, TRACER has sought the consent of counsel for all parties. All parties save respondents, the North American Telephone Association and the United Telephone Company have consented.

1. TRACER is an unincorporated association of 27 business customers of local telephone companies regulated by the public service commissions of Oregon, Washington, Idaho and Nevada. Members of TRACER represent nearly every major segment of Pacific Northwest business, including local and interstate financial services, retail and commercial enterprises, manufacturing, large and small hospitals and local and regional governments. Collectively, TRACER members pay approximately $54 million each year for intrastate telecommunications services. Members of TRACER meet regularly to review current developments in the telecommunications industry, to exchange information on telecommunications issues and concerns and to evaluate the impacts of state and federal governmental initiatives concerning telecommunications. Where appropriate, TRACER has intervened in both state and federal regulatory proceedings, to provide regulatory agencies with information concerning the views of the business community on proposed telecommunications tariffs and policies, and to provide these agencies with independent analyses of the justifications for or the impacts of the proposals

2. In the case at bar, the lower court upheld the Federal Communications Commission's preemption of state prescription of depreciation rates used in setting intrastate telephone rates. In preempting state regulation of depreciation rates, the FCC ordered that all telephone companies be permitted to apply a method of accounting which results in more rapid capital re-

covery and, as a consequence, substantial rate increases for local telephone services.

3. The lower court's decision, if upheld, would produce substantial increases in telecommunications service rates for TRACER members. The rate increases will raise costs of production for TRACER members, producing higher prices for goods and services. Moreover, these rate increases will produce greater incentives for TRACER members to invest in alternative ("bypass") telecommunications systems, resulting in revenue losses to local telephone companies, loss of subscribership to the local network and deterioration of service quality to both residential and business customers.

4. TRACER is aware of no other party, intervenor, or amicus representing the interests of business ratepayers. TRACER has reason to believe that no other party to this proceeding will present arguments concerning the validity and impact of the lower court's decision in precisely the same manner as is set forth in the attached brief. In particular, TRACER knows of no other party that will present the impact of the FCC's preemption order on consumers, business or residential.

WHEREFORE, TRACER respectfully requests leave of the Court to file its brief as amicus curiae.

Respectfully submitted

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INTEREST OF AMICUS CURIAE

The interest of the Telephone Ratepayers Association for Cost-based and Equitable Rates (TRACER) as amicus curiae is set forth in the motion for leave to file that accompanies this brief.

SUMMARY OF ARGUMENT

Federal agency preemption is valid only if an agency can demonstrate that Congress "unmistakably . . . ordained" the preemptive action or that "the nature of the regulated subject matter permits no other conclusion." *Florida Lime and Avocado Growers, Inc.* v. *Paul*, 373 U.S. 132, 142 (1963).

The FCC's preemption of state depreciation regulation satisfies neither of these requirements. Congress did not expressly preempt state regulatory authority over depreciation rates in the Federal Communications Act, 47 U.S.C. § 151 *et seq.* Instead, it created a system of joint regulation by federal and state authority specifically designed to avoid excessive federal encroachment into areas of traditional state concern. 47 U.S.C. §§ 152(b), 220(b), 221(b).

Moreover, the nature of telecommunications regulation does not require federal preemption. Continued state regulation of depreciation presents no direct conflict with any lawful policy or objective of the FCC. Quite the opposite is the case. State regulation of depreciation is consistent with over forty years of FCC practice and comports with federal directives concerning the maintenance of an efficient nationwide network of telecommunications services. Federal preemption, on the other hand, conflicts with longstanding practice and threatens the very competitive telecommunications environment that the FCC has worked so long to foster.

For these reasons, the lower court's ruling approving the FCC's preemption of intrastate ratemaking should be reversed.

ARGUMENT

A. Introduction

At issue in this case is a 1983 Federal Communications Commission order requiring states to allow local telephone companies to use several specific methods of computing depreciation of telephone equipment and other investments. These methods, in large part, result in faster depreciation of telecommunications investments.[1] To support its preemption of what had been theretofore regulated by state regulatory commis-

[1] The primary method allowed by the FCC involved the "grouping" of investments (e.g. telephone poles, switches, cables) for the purpose of calculating service lives, the periods of time over which the costs of the investments can be recovered. Until the FCC's 1983 order, investments were grouped according to the year of installation and depreciated over the average service life of those investments, even though wide variations in actual service lives existed.

In its preemption order, the FCC allowed "equal life grouping." Under this method, investments are grouped according to their actual expected service lives, regardless of the year of installation. Smaller investment groups result, and theoretically, capital recovery better matches actual service lives.

On the average, the use of equal life grouping results in faster depreciation of investments, particularly if service lives are adjusted to reflect technological — as opposed to physical — obsolescence.

In its 1983 order, the FCC also allowed the use of the "remaining life" method to accommodate such adjustments. (footnote carried forward)

sions, the FCC relied on two theories. First, the agency argued that the Federal Communications Act, 47 U.S.C. § 151 *et seq.*, expressly authorized such preemption. *Amendment of Part 31*, 92 F.C.C.2d 864, 869 (1983). Second, it argued that if the states refused to allow the specific depreciation practices mandated, local telephone companies would fail to invest in new technology and competition in the interstate telecommunications marketplace would suffer. *Id.* at 876-77.

The Court of Appeals for the Fourth Circuit affirmed, albeit over a vigorous dissent. *Virginia State Corporation Commission* v. *Federal Communications Commission*, 737 F.2d 388 (4th Cir. 1984). In upholding the FCC's preemptive order, however, the lower court misapplied longstanding precedent governing preemption of state authority by federal agencies.

Settled principles of constitutional law require federal agencies to satisfy stringent requirements before they may preempt state regulatory authority. This is particularly true in the case of federal regulation of trade and commerce. As the Court recently stated in *Hayfield Northern Railroad Company* v. *Chicago and Northwestern Transportation Company*, — U.S. —, 52

(footnote continued)

Under this method, a company may simply allocate any unrecovered depreciation over the remaining adjusted service life of the investment. Again, if the adjustments are made to reflect technological obsolescence, depreciation tends to be substantially accelerated under this method. *See generally Amendment of Part 31*, 83 F.C.C.2d 267 (1980).

U.S.L.W. 4783, 4786 (June 12, 1984), "federal regulation in a field of commerce should not be deemed preemptive of state regulatory power in the absence of persuasive reasons — either that the nature of the regulated subject matter permits no other conclusion or that Congress has unmistakably so ordained." (quoting *Florida Lime and Avocado Growers, Inc.* v. *Paul*, 373 U.S. 132, 142 (1963)). *See also Fidelity Federal Savings & Loan Association* v. *de la Cuesta*, 458 U.S. 141, 153 (1982).

Whether Congress has "unmistakably . . . ordained" federal preemption is ultimately a question of congressional intent, which may be explicitly stated in a "statute's language or implicitly contained in its structure and purpose." *Jones* v. *Rath Packing Co.*, 430 U.S. 519, 525 (1977).

Whether "the nature of the regulated subject matter permits no other conclusion" may be determined by the existence of direct conflicts with federal law, either when "compliance with both federal and state regulations is a physical impossibility," *Florida Lime*, 373 U.S. at 142-43, or when state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Hines* v. *Davidowitz*, 312 U.S. 52, 67 (1941); *see also de la Cuesta*, 458 U.S. at 153.

The FCC's preemption of intrastate ratemaking fails to satisfy these essential qualifications for valid federal agency preemption. Congress has not unmis-

takably ordained that the FCC must preempt state authority over telephone rates. Neither does the existence of differing state depreciation ratemaking practices conflict with any of the FCC's statutory purposes or objectives. There being no valid reason for the FCC to exercise such extraordinary preemptive authority, the lower court's decision upholding the FCC's preemption order should be reversed.

B. Congress Has Not "Unmistakably Ordained" That State Ratemaking Authority Should Be Preempted.

Nothing in the Federal Communications Act, 47 U.S.C. § 151 *et seq.*, evinces unmistakable congressional intent that state regulators should not be allowed to fashion telephone rates to reflect the needs and conditions of their own jurisdictions. On the contrary, careful scrutiny of the Act and its legislative history reveals that Congress created a system of shared authority to be jointly exercised by the FCC and the states.

The Act does give the FCC certain powers to set depreciation charges.[2] However, section 152(b) also

[2] Section 220(b) states that

> The Commission shall, as soon as practicable, prescribe for such carriers the classes of property for which depreciation charges may be properly included under operating expenses, and the percentages of depreciation which shall be charged with respect to each of such classes of property, classifying the carriers as it may deem proper for this purpose.

47 U.S.C. § 220(b).

expressly reserves for the states authority to regulate intrastate telecommunications services:

> [N]othing in this chapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service . . .

47 U.S.C. § 152(b). Similarly, section 221(b) provides that the FCC's jurisdiction cannot infringe upon "matters . . . subject to regulation by a state commission or by local government authority." 47 U.S.C. § 221(b). Thus it is clear from the language of the Act itself that the FCC was not intended to be the sole arbiter of telecommunications service charges and classifications. This authority was intended to be shared.

The legislative history of the Communications Act illuminates Congress's intent to limit FCC incursions into state ratemaking practices. Prior to passage of the 1934 legislation, the Supreme Court had authorized the Interstate Commerce Commission to set intrastate railroad rates to avoid discrimination between state and federal rates. *Houston, East & West Texas Railway Co.* v. *United States*, 234 U.S. 342, 358-59 (1914) (the "*Shreveport Rate Case*"). Concerned about this extraordinary grant of federal agency authority, Congress crafted the Communications Act to preserve shared federal and state responsibility for regulating telecommunications rates and charges. In the 1934 Senate Committee hearings, for example, the chairman of the Interstate Commerce Committee plainly stated

that the Committee's legislation was written "to protect the state commissions against being overridden by this Commission, as the Interstate Commerce Commission has overridden some of the railroad state commissions." *Hearings on S. 2910 before the Senate Interstate Commerce Committee*, 73rd Cong., 2d Sess. 179 (1934) (Statement of Senator Dill). *See also North Carolina Utilities Commission* v. *Federal Communications Commission*, 552 F.2d 1036, 1047 (4th Cir. 1977) ("[I]n enacting the Communications Act, Congress sought to deny the FCC the kind of jurisdiction over local rates approved by the *Shreveport Rate Case*.").

For over forty years the FCC exercised its authority consistent with this principle of shared jurisdiction. Indeed, as late as eight months prior to the preemption order at issue in this case, the agency commented that the language of the Communications Act indicated that

> the 1934 Congress wished to achieve as much uniformity as possible without coercing any state commission to use ratemaking methods it found acceptable. This commission has proceeded in a manner that is consistent with that purpose for nearly four decades. We have always given special consideration to the needs and views of State commissions in developing accounting and depreciation rules and most State commissions have chosen to follow most accounting and depreciation rules prescribed by this commission. Departures have nonetheless occurred from time to time.

> This Commission has never attempted to prevent any State commission from departing from our accounting and depreciation rules. *Indeed, we have expressly recognized that State commissions have a right to do so.*

Amendment of Part 31, 89 F.C.C.2d 1094, 1106-07 (1982) (emphasis added).[3]

To say that Congress has "unmistakably ordained" federal preemption of state depreciation ratemaking does unconscionable violence to the explicit language of the Federal Communications Act, its legislative history, and over forty years of consistent, uninterrupted interpretation by the FCC itself. The lower court's approval of the FCC's preemption order should be reversed and the states restored their statutory and historical right to set local telephone rates.

C. State Regulation of Local Depreciation Rates Does Not Directly Conflict With The Purposes And Objectives of Lawful Federal Communications Regulation.

Only when there is a direct conflict with federal authority can an agency of the federal government

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[3] In the same order, the FCC further observed that to preempt state depreciation regulation would

> repudiate nearly forty years of administrative practice and applicable state court proceedings by adopting an interpretation of Section 220 that would require an unwilling state commission to follow all accounting and depreciation methods prescribed by this Commission. A very compelling showing would be required to persuade us to follow such a course.

Amendment of Part 31, 89 F.C.C.2d at 1107.

presume upon the jurisdiction of the states. State law must do "'major damage' to 'clear and substantial' federal interests before the Supremacy Clause will demand that state law be overridden." *Hisquierdo* v. *Hisquierdo*, 439 U.S. 572, 581 (1979) (quoting *United States* v. *Yazell*, 382 U.S. 341, 352 (1966)). Mere theoretical inconsistencies will not suffice. *Hayfield*, 52 U.S.L.W. at 4786.

No conflict with federal interests exists here. Absolutely nothing in any of the FCC's recent orders concerning depreciation ratemaking demonstrates that state and federal regulation of telephone depreciation practices cannot lawfully co-exist.

According to the FCC, preemption is necessary to ensure that improper capital recovery at the local level does not frustrate investment in developing technology and thus impede an interstate carrier's ability to compete with new entrants in the interstate marketplace.[4] And competition, the FCC has determined, is the optimum method of fulfilling its statutory responsibility to provide a "rapid, efficient, nationwide, and world-wide" communications network. *Amendment of Part 31*, 92 F.C.C.2d at 876-877.

It may be true that local depreciation practices

[4] According to the FCC, failure to allow equal life group and remaining life methods could hamper carriers' ability to raise sufficient capital to invest in more modern equipment, needed "to fully compete in the continually evolving competitive telecommunications marketplace." *Amendment of Part 31*, 92 F.C.C.2d at 877.

have some effect on the extent to which local exchange companies upgrade telephone plant and invest in new technology. But the connection between technological advances at the local level and the existence of competition on an interstate basis is all but impossible to discern.

The problem with the FCC's argument is that it ignores the fact that local exchange companies are required to provide access to competing carriers on an equal basis. *United States* v. *American Telephone and Telegraph Company*, 552 F. Supp. 131, 196 (D.D.C. 1982), *aff'd*, — U.S. —, 103 S. Ct. 1240 (1983). This is true regardless of the local companies' depreciation practices or the technologies in which they choose to invest.

If, for instance, a local telephone company is required to use a less detailed form of depreciation and it is unable to finance the purchase of new switching technology, interstate carrier competition is not affected in the least. Each interstate carrier connects its transmission lines to the very same local switching equipment. None is given a competitive advantage over the other.

Likewise, if the FCC-mandated depreciation methods are adopted and the local company is able to finance the purchase of the latest digital electronic switching systems, the result is exactly the same. The interstate carriers have access to the identical technology. Their ability to compete with one another re-

mains unaffected. In short, whether a state chooses to allow one method of depreciation or another, its decision will have no impact on the relative competitive positions of interstate carries whatsoever. [5]

If state regulation of depreciation charges has any impact on competition in the telecommunications markets at all, it is on intrastate markets alone. Fostering competition within purely intrastate markets is, however, beyond the express statutory authority of the FCC. 47 U.S.C. § 152(b). Even under the agency's own interpretation of the Act, the FCC would not have the authority to preëmpt state regulatory authority in order to pursue a policy of developing intrastate competition. *See* Motion to Dismiss and Brief for the Federal Respondents in Opposition at 15 (section 152(b) "preserves state authority over purely intrastate matters . . .").

This is as it should be, for the states are in the best position to evaluate local market conditions, customer demands and other economic realities that bear upon the appropriateness of varying regulatory approaches to the telecommunications industry. In some areas of Eastern Oregon and Washington and Northern Idaho, for example, competition for telecommunications services of any sort is virtually non-existent. In contrast, major metropolitan areas such as Seattle and Portland experience burgeoning competition for a variety of telecommunications services. A federal agency is simply not equipped with the information necessary to develop a system of telecommunications regulation that best suits the needs of local ratepayers.

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[5] In his dissent from the lower court's affirmance of the FCC's depreciation order, Judge Widener expressed similar skepticism at the agency's argument:

> I cannot see how nonconforming depreciation methods for the carriers' intrastate operations can frustrate competition in the interstate communications markets within which there is competition. The only rationale I can find for the FCC's position is that the States, if not required to follow the FCC's lead, will allow the carriers less revenue . . .

Virginia State Corporation Commission v. *Federal Communications Commission*, 737 F.2d 388, 398 (Widener, dissenting).

And the states are facing up to their task. The FCC has not stepped in to fill a regulatory void. In the Pacific Northwest, the legislatures of Oregon and Washington have this last year enacted sweeping new laws that allow state regulatory authorities to regulate, deregulate, or detariff telecommunications services to meet current market conditions. The Public Utilities Commission of Idaho is currently evaluating appropriate standards to be used in determining when the public interest would be served by relaxed forms of telephone company regulation. Similarly, the Nevada Public Service Commission has recently initiated a rulemaking proceeding to determine the extent to which intrastate competition exists in that area and how it should be regulated. Thus, not only is FCC interference with state ratemaking authority illegal, it is unnecessary.

Even if the FCC were correct in asserting that state depreciation regulation directly affects interstate competition, closer scrutiny of the facts discloses that the ultimate affect is exactly the opposite of what the FCC supposes. Rather than present a conflict with lawful federal objectives, state depreciation regulation is perfectly consistent with the FCC's competitive objectives. It is the federal preemption of depreciation ratemaking that will frustrate the creation of competitive markets.

To achieve the goal of engendering a dynamic, competitive telecommunications marketplace, the FCC has required that states authorize telephone companies to use depreciation methods that accelerate the recovery of investments in telephone plant. Using the accelerated recovery methods, however, necessarily produces sizeable rate increases for ratepayers. [6] The FCC's own estimates of the impact of its preemption order total over $2 billion for 1984 alone. W. Bolter, *Telecommunications Policy for the 1980s: The Transition to Competition* 166 (1984). In a single South Central Bell rate case, the FCC's required depreciation practices produced rate increases totaling

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6 According to basic principles of public utility ratemaking, each year a telephone company deducts the allowable sum for depreciation from its rate base and charges the sum as an operating expense, that is, as a direct addition to the company's revenue requirement. *See generally* C. Phillips, *The Regulation of Public Utilities* 250-57 (1984). Thus, if the company is allowed to depreciate a greater sum over a shorter period of time, larger revenue requirements result.

over $60 million. *See* Jurisdictional Statement of Louisiana Public Service Commission at 16. [7]

It is hard to imagine how such increases in consumer rates would make the regulated telephone companies better equipped to deal with growing competition. Basic economics and actual experience indicate that such increases in telecommunications service rates provide high-volume business customers with significant incentives to bypass local networks, resulting in still higher rates as fewer customers are left to pay for the largely fixed costs of the system. [8] If anything, the FCC's preemption of state depreciation ratemaking will itself thwart the development of competition. [9]

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7 The so-called Ernst Report, "Study of Depreciation Rate Practices and Policies," prepared for the FCC in its original evaluation of depreciation practices, conceded that the use of depreciation procedures ultimately mandated by the agency "would result in increases in revenue requirements initially, and possibly over the longer term . . ." *Amendment of Part 31*, 83 F.C.C.2d 267, 279 (1980). The Ernst Report also added that the use of this methodology "would result in an increased regulatory burden and consequently, increased regulatory staffs." *Id.*

8 Pacific Northwest Bell estimates that from local ("intra-LATA") bypass alone, it faces a potential revenue loss of over $44 million. Pacific Northwest Bell, *Bypass Analysis* 30 (May 16, 1984). Rate increases required to cover increased depreciation expenses can only serve to increase the amount at risk.

9 The fact that the FCC believes that local exchanges can withstand the price increases also belies the agency's unsubstantiated conclusion that competition even exists on a widespread basis. Any effort at accelerating capital recovery requires captive — monopoly — ratepayers that can tolerate

Even worse, federal preemption of depreciation ratemaking will lead to inefficient and costly overinvestment, producing systems top-heavy with esoteric technology of little use to most subscribers. It is no coincidence that Pacific Northwest Bell — during the most recent depreciation ratesetting proceeding — announced its plans to invest in 145 state-of-the-art electronic digital switching systems, to be installed in predominantly rural areas of Western Washington and Oregon at a total cost of $102 million. The benefits to a competitive telecommunications market are dubious at best. But the impact on telephone service rates will be unmistakable. [10]

(Footnote continued)

the increases. Otherwise, customers would seek alternative providers not burdened with the costly problem of speeding up plant turnover. See Trebing, *A Critique of Structure Regulation in Common Carrier Telecommunications*, in Telecommunications Regulation Today and Tomorrow (E. Noam ed. 1983) 145-46.

[10] TRACER is certainly aware that its members — many of whom are large, high volume business customers — stand to benefit from the installation of efficient, up-to-date network equipment. However, the specific demands of these customers, the threat of bypass, market conditions, and other factors with which state regulators are routinely familiar, are more than adequate to ensure timely upgrading of plant quality. The FCC's unwarranted penchant for national uniformity merely encourages local companies in all areas to rapidly convert their networks, whether customers would benefit or not, all at great expense to business and residential ratepayers, large users and small.

CONCLUSION

The Federal Communications Commission's preemption of state depreciation regulation is illegal and unnecessary. It is supported by neither the language of the Communications Act, the legislative history, nor sound ratemaking policy. In approving the FCC's preemption order the lower court erred, departing from a long line of authorities on the requirements of valid federal agency preemption.

For the foregoing reasons, TRACER as amicus curiae urges the Court to reverse the judgment of the court below.

Respectfully submitted

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